[redacted]

NO. 240

J. VIRGIL SCOTT, ET AL., and PAUL A. SCOTT, ET AL., *Appellants*,

v.

UNION PRODUCING COMPANY, ET AL., *Appellees*.

SUPPLEMENTAL REPLY TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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IN THE

Supreme Court of the United States

October Term 1959

NO. 340

J. VIRGIL SCOTT, ET AL., and PAUL J. ROGERS, ET AL., *Appellants*

v.

UNION PRODUCING COMPANY, ET AL., *Appellees*

SUPPLEMENTAL REPLY TO APPELLANTS' PETITION FOR WRIT OF CERTIORARI

Statement

Appellee-Respondents, Claire H. Parmelee and husband, Clyde D. Parmelee, J. J. Burdin, Horace Etchison, G. G. Sueyasu and wife Asao Sueyasu, respectfully ask leave of the Honorable Court to submit this their Supplemental Reply to the Petition of J. Virgil Scott, et al. for a writ of certiorari in the above styled and numbered cause.

Since the filing of their original Reply to said Petition the Supreme Court of Texas has handed down its opinion in the case of *Gulf Oil Corporation v. E. L. Reid*,

a certified copy of which opinion is hereto annexed as Appendix A, and is, we submit, determinative of the case at bar.

Argument

As shown on its face, said opinion in the *Reid* case, rendered on March 23, 1960, squarely reaffirms, supports and applies the ruling of the Supreme Court of Texas in the case of *Freeman v. Magnolia Petroleum Oil Company*, 141 Tex. 274, 171 S.W. 2d 339 (Tex. Sup. 1943), cited and relied upon by these Respondents at pages 12 and 13 of their original Reply. As explicitly stated by the Supreme Court of Texas in the later case of *Rogers v. Osborn*, 152 Tex. 540, 261 S.W. 2d 311 (Tex. Sup. 1953), the ratio decidendi of the *Freeman* case is as follows:

> "And we have held that where the 'year' of this shut-in gas royalty clause straddles the date for expiration of the primary term, the shut-in payment must be made during the primary term, or the lease expires. Freeman v. Magnolia Petroleum Co., supra."
>
> *Rogers v. Osborn*, supra, P. 313.

In the *Reid* case a well capable of production was brought in on January 18, 1949, and was capped on that date for want of market facilities. On February 19, 1949, which was after the end of the primary term of the lease, the lessee tendered the "shut-in" gas royalty payment. Thereafter, on November 22, 1949, gathering lines were laid and connected, and from then on until the date of trial the well continued to produce in paying quantities. The lessee contended that since the "shut in" well payment was tendered within the time allowed for such payments, the lease was continued in force and effect.

In answering this contention of the lessee in the *Reid* case the Supreme Court of Texas said:

> "Just as the provisions in this lease have been held to deny a reasonable time to find a market after discovery of oil, so they have been construed to deny a reasonable time within which to pay 'shut-in' royalty after the 'shut-in' has taken place. This was explicitly held in *Freeman v. Magnolia*, supra, under similar facts, practically the only distinction being that in Freeman the discovery well had been brought in a few months prior to the end of the primary term. Gas was discovered in large quantities but none was used or sold off the premises. The 'shut-in' royalty was not tendered for more than four months after the end of the primary term. The lease lapsed as a matter of law, there being no gas produced from the premises on the last day of the primary term, and the royalty not having been paid on or before that date. The lease could not be revived by an attempt to pay the royalty four months thereafter."
>
> Appendix A, p. 13.

Thus the lease in the *Reid* case, as in the *Freeman* case, was held to have lapsed since the substitute production payment relied upon was not tendered before the end of the primary term even though tendered within the period allowed by the lease for "shut-in" well payments generally.

This we submit is the law of Texas, as laid down by the Supreme Court of that state.

In the case at bar the "shut-in" well payments, even if such substitute production were permitted under the provisions of the term grants here involved (which is expressly denied), came too late, for they were tendered some three months after the lapse of the term grants on October 25, 1955. (R. 149-150, 183-184.)

It is submitted, therefore, that regardless of what view this Court may take on the question whether a substitute production provision was written into Petitioners' term grants, the tender of substitute production herein shown came too late, since admittedly it was not made until some three months after the termination of Petitioners' term grants on October 25, 1955.

Neither of the lower Federal courts found it necessary to pass upon this question, since both courts held that no provision for substitute production had been written into Petitioners' limited term grants, and therefore the term grants had lapsed on October 25, 1955.

The rationale of these holdings of the Supreme Court of Texas is that where substitute production is allowed in a lease or term grant, such substitute production sought to be brought into effect after the lapse of the primary term cannot keep alive that which is already dead.

This eminently sound rule of law squarely applies to the case at bar wherein the well capable of production was completed on October 17, 1955, and capped on October 23, 1955. On October 25, 1955, the term grants expired for want of production at that time. The attempted "shut-in" well payment was not tendered until after January 17, 1956. (R. 146, 183; 144, 145.) Even if such tender was made within the quarterly period after completion allowed by the lease for the making of "shut-in" well payments, nevertheless under the plain rule of the *Freeman* case it could not revive the term grants which had already lapsed.

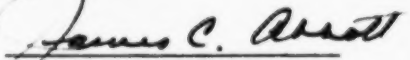
As heretofore stated, neither of the lower courts found it necessary to apply this rule of the *Freeman* case, inasmuch as they both held that there was no provision for substitute production in appellants' term grants. Even

if this Court should disagree with the two lower courts on this point, it would be a needless exercise of the power to grant writ of certiorari herein, or to remand the case, when the Supreme Court of Texas has so explicitly laid down the law of that state applicable to substitute production sought to be invoked after the termination date of the limited estate.

Conclusion

For all of the foregoing reasons Respondents say that the Petition for Writ of Certiorari should be dismissed.

Respectfully submitted,



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Certificate of Service

Copies of the above and foregoing Supplemental Reply to Petition for Writ of Certiorari have been served on all counsel for Petitioners herein, and Mr. W. S. Stovall, pro se, prior to the filing hereof.

Dated: April 28, 1960.

James C. Abbott

JAMES C. ABBOTT

APPENDIX A

NO. A-7343

IN THE SUPREME COURT OF TEXAS

GULF OIL CORPORATION, Petitioner	§	From Orange County,
v.	§	Ninth District
E. L. REID, Respondent	§	

The chief question presented here is whether the so-called "shut-in" royalty payment, tendered after a well capable of producing gas only in paying quantities had been capped, was so timely made as to extend the term of an oil and gas lease after the expiration of the primary term.

On December 9, 1943 E. L. Reid, who owned an undivided 1/8th mineral interest, executed to Gulf Oil Corporation an oil and gas lease for a primary term of five years. Gulf began the drilling of a well a few days before expiration of the primary term and continued drilling operations up to and including January 18, 1949, subsequent to the end of the primary term when the well in question was completed. This well, which was capable of production in paying quantities, was capped on that date due to the lack of market facilities. On February 19, 1949, Gulf tendered the "shut-in" gas royalty payment to Reid, which was rejected by him. On June 7, 1949, Gulf con-

tracted with a pipe line company for the sale and purchase of the gas. On November 22, 1949, the gathering lines had been laid and connected, and thereafter until the date of the trial of this case the well has continued to produce in paying quantities.

This suit was filed by E. L. Reid seeking to have the Court decree that the lease terminated under its own provisions and for recovery of title to and possession of his undivided 1/8th interest in the minerals, and for an accounting. The trial court denied the relief sought, and held the mineral lease to be in full force and effect. The Court of Civil Appeals reversed and remanded. 323 S.W. (2) 107. The applications for writ of error of both parties are before us. We will direct our attention first to that of Gulf Oil Corporation.

Petitioner asserts: (1) That it had a reasonable time to obtain a market for its gas from and after the completion of the well, (2) that inasmuch as no time was expressly provided within which the royalty must be paid, the only stated condition being that $50.00 be paid per well per year, by implication the lessee could pay the royalty at any time within the year following the "shut-in" of the well; (3) that there was actual production of gas within the terms of the lease; (4) that there was thereafter a cessation of production within the meaning of paragraph 5 of the lease so as to bring into play the 60-day cessation-of-production provision and thus keep the lease alive for a period of 60 days after the well was capped and production ceased; (5) that the lessee had the privilege of paying the "shut-in" royalty at any time so long as the lease was kept alive under any of its provisions. We think the Court

of Civil Appeals correctly resolved these issues against petitioner's contentions. The lease followed substantially the usual "unless" form.[1]

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1 "2. Subject to the other provisions herein contained, this lease shall be for a term of Five (5) years from this date (called primary term) and as long thereafter as oil, gas or other mineral is produced from said land hereunder, or as long as drilling or reworking operations are being conducted on said land as is hereinafter provided.

"3. * * * where gas from a well producing gas only is not sold or used, Lessee may pay as royalty Fifty Dollars ($50.00) per well per year, and upon such payment it will be considered that gas is being produced within the meaning of Paragraph 2 hereof; * * *.

"5. If, during the primary term and prior to the discovery of any mineral on said land, Lessee should drill a dry hole thereon, this lease shall not terminate if Lessee either commences additional operations for drilling on or before the rental date next ensuing after the expiration of sixty (60) days after the abandonment of said dry hole,/ or commences or resumes the payment or tender of rentals, as hereinabove provided, on or before the rental date next ensuing after the expiration of sixty (60) days after the abandonment of said dry hole. If a dry hole is completed and abandoned during the last period of the primary term, Lessee's rights shall remain in full force and effect without further operations until the expiration of said period. After the discovery of any mineral in paying quantities on the land, all of Lessee's rights shall remain in effect as long as any mineral is produced therefrom; and if, during the primary term, the production of all minerals therefrom should cease from any cause, this lease shall not terminate if Lessee either commences or resumes the payment or tender of rentals, as hereinabove provided, on or before the rental date next ensuing after the expiration of sixty (60) days after the cessation of production, or commences additional drilling or reworking operations on or before said next ensuing rental date. If cessation of production occurs at any time after the expiration of the primary term, then this lease shall not terminate if Lessee, until production is again procured, does not allow more than sixty (60) days to elapse between the cessation of production and

At the outset we will reiterate the following propositions that have been well established during the development of oil and gas law in this State. (1) An oil and gas lease such as the one we have before us created a determinable fee in the land which terminates upon the happening of the events upon which it is limited. Texas Co. v. Davis, 113 Tex. 321, 254 S.W. 304; W. T. Waggoner Estate v. Sigler Oil Co., 19 S.W. 2d 27; Stanolind Oil & Gas Co. v. Barnhill, Tex. Civ. App. err. ref.) 107 S.W. 2d 746; Cox v. Miller, (Tex. Civ. App. err. ref.) 184 S.W. 2d 323; (2) the word "production" as used in the habendum clause of this lease is equivalent to the phrase "production in paying quantities." The term "paying quantities" embraces not only the amount of production, but also the ability to market the product at a profit. Garcia et al v. King et al, 139 Tex. 578, 164 S.W. 2d 509. As said in that case, "the object of the contract was to secure the development of the property for the mutual benefit of the parties. It was contemplated that this would be done during the primary term of the contract." To this sentence we might add the phrase, "or during the extension of the lease term." Thus,

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the commencement of additional drilling or reworking operations in a bona fide effort to again obtain production, and successive attempts may be made so long as not more than sixty (60) days are allowed to elapse between the completion or abandonment of one well and the commencement of operations on another until production is again obtained. If, at the expiration of the primary term, oil, gas or other mineral is not being produced from the land then covered hereby, but Lessee is then engaged in operations for drilling or reworking operations on some part of the land hereunder, this lease shall not terminate if Lessee does not allow more than sixty (60) days to elapse between the abandonment of one well and the commencement of drilling or reworking operations on another until production is obtained."

no matter how great the potential production may be or how many million cubic feet of gas may have been flared, there would be no production or production in paying quantities unless there was an available market; (3) the fact that there is no available market is not an excuse for failure to produce, and the lease terminates unless some other provision will keep it in force. Rogers v. Osborn, 152 Tex. 540, 261 S.W. 2d 311; Stanolind Oil & Gas Co. v. Barnhill, supra; Watson v. Rochmill, 137 Tex. 565, 155 S.W. 2d 783; Freeman v. Magnolia Petroleum Co., 141 Tex. 274, 171 S.W. 2d 339; W. T. Waggoner Estate v. Sigler Oil Co., supra; Cox v. Miller, supra; Holchak v. Clark, 284 S.W. 2d 399 (Tex. Civ. App. err. ref.); Sellers v. Breidenbach, 300 S.W. 2d 178, (Tex. Civ. App. err. ref.).

The recital of these principles without further elaboration might well be sufficient to demonstrate the fallacy of Gulf's contention in this case.

The trial court, inter alia, made the following findings of fact: (1) No gas was sold from the well until November 22, 1949, when actual deliveries were made to the pipe line company; (2) Gulf was at all times diligent in attempting to secure a purchaser for the gas from this well and in expediting the completion of the pipe line company's facilities and connections; (3) that the marketing of the production from the lease was accomplished within a reasonable time after the completion of the well; (4) that the "shut-in" royalty payment was made within a reasonable time; (5) that the plaintiff had not ratified the lease after the completion of the well and is not estopped from urging that the lease has terminated.

In support of its contention that the lease is kept alive for a reasonable length of time to permit lessee to find a market, Gulf relies on Union Oil Company of California v. Ogden, (Tex. Civ. App.) 278 S.W. 2d 246 (wr. ref. n.r.e.). The Court does say in that case that the lessee should have a reasonable time to market the gas even though that time would extend beyond the primary term. It defines, however, "a reasonable time" as that time necessary for the lessee to lay gathering lines to the available market, saying that it was necessary for the lessee "to forthwith begin operations for laying the line and continue such operations with reasonable diligence and dispatch until the gas reached the market." In the absence of those operations the lease was held to be terminated. That decision only supports the holding of the Court of Civil Appeals in our case to the effect that laying extensions and connections from the well to the pipe line by the lessee are to be classified as drilling operations. That question we do not reach. The efforts of Gulf consisted solely of negotiations with the pipe line company and no manual operations were conducted by either Gulf or the pipe line company until some time after the June 7th contract.

The authorities hold to the contrary of Gulf's position here. In Holchak v. Clark, supra, the trial court thought as a matter of law that the discovery of oil kept the term "royalty deed" alive for a reasonable time after its termination date for the purpose of determining whether or not the well would produce in paying quantities. In reversing, the Court of Civil Appeals held that as there was no paying production from the premises at the end of the term, the mineral estate reverted to the grantors. To the same effect is the decision in Sellers v. Breidenbach, supra.

Just as the provisions in this lease have been held to deny a reasonable time to find a market after discovery of oil, so they have been construed to deny a reasonable time within which to pay "shut-in" royalty after the "shut-in" has taken place. This was explicitly held in Freeman v. Magnolia, supra, under similar facts, practically the only distinction being that in Freeman the discovery well had been brought in a few months prior to the end of the primary term. Gas was discovered in large quantities but none was used or sold off the premises. The "shut-in" royalty was not tendered for more than four months after the end of the primary term. The lease lapsed as a matter of law, there being no gas produced from the premises on the last day of the primary term, and the royalty not having been paid on or before that date. The lease could not be revived by an attempt to pay the royalty four months thereafter.

The provision in the lease for the payment of "shut-in" royalty is to provide for just that eventuality, namely, where gas has been discovered in paying quantities, but a market is lacking. This rule applies with equal force to the claim that the royalty payment could be tendered at any time within the period of one year after the well had been capped or "shut-in". Courts will not rewrite an oil and gas lease to provide that production, actual or contractual, will operate to extend its life when it has terminated by its provisions.

Gulf seeks to invoke the application for the "60-day-cease-to-produce clause" and says that, since the well did *in fact* produce gas in substantial quantities and was subsequently "shut-in", it therefore *ceased* to produce. Although this well was capable of producing in paying quantities, considerable gas having been flared and an undis-

closed number of barrels of condensate obtained, none was ever sold or used on or off the premises. Therefore, under the authorities cited above there was no production from the well within the meaning of the lease provisions. It follows, that since there had been no production, there could not be a cessation of production, and thus the 60-day clause is not available to the petitioner to extend the term of the lease or to delay the tender of the royalty payment. While petitioner discusses a number of cases under this point, and urges the matter with considerable force and logic, we are of the opinion that the question is foreclosed to the contrary. Actually the only case Gulf relies on as supporting its position is that of Shell Oil Co. v. Goodroe, 197 S.W. 2d 395 (wr. ref. n.r.e.). There the tender of "shut-in" royalty was not made before Shell had capped and shut-in the gas well. The case is distinguished, however, on several grounds. In the first place gas and condensate had been marketed from the well and the "shut-in" royalty payment was tendered within the 90-day period after production had ceased in compliance with the terms of the lease. In the second place, the royalty payment was not only tendered, but was accepted by the lessors and therefore the decision, we think, has little bearing on the problem presented here.

The last provision in Section 5 of the lease will not support petitioner's theory that it permitted payment of "shut-in" royalty at any time within a period of 60 days after the well was capped. Petitioner argues that the meaning of this provision was to allow a period of 60 days after the completion date of the well either to bring in actual production or pay royalty in lieu thereof or to abandon further operations on that well and commence additional operations on another. What we think petitioner is actually

saying is, that after the completion of the well, the provision grants additional time within which to determine whether the well is to be abandoned or not. Here there was no question at any time as to abandonment. It was capped only because of the lack of market facilities. In the usual course of development, operations normally would continue to make the well productive until the decision to abandon is made. The lease provision means what it says, namely, that in the event of abandonment the lessee has 60 days within which to decide on his further course. To adopt the meaning ascribed to it by Gulf would be to compel a strained and unnatural construction. To sum up, there was no production from the well during the term of the lease as extended by drilling operations; the "shut-in" royalty was not paid so as to bring about constructive or contractual production, and no provisions of the lease can be construed to furnish a further extension of the primary term or to make the tender of royalty in this case timely.

We now pass to the points raised by the lessor, Reid, in his application. He contends that the Court of Civil Appeals erred in remanding the case for another trial. To arrive at that result the Court of Civil Appeals reasons that when paragraph 2 and the last provision of paragraph 5 are considered together the latter provision should be construed to read: "If, at the expiration of the primary term, oil, gas or other mineral is not being produced from the land then covered hereby, but lessee is then engaged in operations for drilling or reworking operations on some part of the land hereunder, this lease shall not terminate so long as said operations shall continue." So the Court apparently thought that a fact question, not passed upon by the trial court, was raised as to whether or not the lessee, after capping the well, prosecuted "drilling opera-

tions" with due diligence measured by common-law standards and further that as to that fact the case had not been fully developed. The trial court had held that the lessee had at all times exercised due diligence in its efforts to provide a market and that these efforts culminated successfully in obtaining the pipe line company to lay and connect its gathering lines to the well. But these efforts, however, merely consisted of negotiations and not in any manual operations on the part of the lessee. In the light of settled rules we think the term "operations" cannot be extended to include a search on the part of lessee for a market or to secure a purchaser. If we accept, as we must, the conclusion that there was no production, therefore, no cessation of production and no abandonment, then in this case it necessarily follows that there was a gap between the completion of the well and production, and the lease terminated. We think, therefore, that the Court of Civil Appeals was in error in remanding the case for the determination of the fact question of diligence.

The last point raised by the lessor, Reid, is to the effect that the Court of Civil Appeals failed to render judgment in his favor as to 1/8th of the net value of the gas and condensate produced by the lessee. This concerns the question as to what credits, if any, are to be allowed to the lessee in equity for the lessor's proportionate part of the expenses incurred by lessee in obtaining production. Lessor's contention is that he became a tenant in common with Gulf when his lease expired and therefore he is proportionately liable for maintenance and marketing expenses from the time that relationship began, but that he is not to be held for any part of the costs of drilling operations and the completion of the well in the first place. This point has not been passed upon by either the trial court

or the Court of Civil Appeals, nor is the point briefed here. We therefore concur in the remand to the trial court, but only for the purposes of determining this question.

The judgment of the Court of Civil Appeals is affirmed.

/s/ FRANK P. CULVER, JR.

Frank P. Culver, Jr.
Associate Justice

Opinion delivered:
March 23, 1960

CLERK'S CERTIFICATE

I, GEO. H. TEMPLIN, Clerk of the Supreme Court of Texas, do hereby certify that the attached and foregoing eight (8) pages contain a true and correct copy of the OPINION delivered by the Supreme Court of Texas in Cause No. A-7343, styled Gulf Oil Corporation vs. E. L. Reid, as the original of the same appears on file and of record in this office.

IN TESTIMONY WHEREOF witness my hand and the seal of the Supreme Court of Texas, at the City of Austin, this the 6th day of April, 1960.

GEO. H. TEMPLIN
Clerk of the Supreme Court
of Texas.

(SEAL)